

Message Text

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ACTION ARA-10

INFO OCT-01 ISO-00 SSO-00 NSCE-00 USIE-00 INRE-00 ERDA-05

AID-05 CEA-01 CIAE-00 CIEP-01 COME-00 DODE-00 EB-07

FPC-01 H-02 INR-07 INT-05 L-02 NSAE-00 NSC-05 OMB-01

PM-03 SAM-01 OES-03 SP-02 SS-15 STR-01 TRSE-00 FRB-03

FEA-01 PA-01 PRS-01 /084 W

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O 132046Z MAR 75

FM AMEMBASSY CARACAS

TO SECSTATE WASHDC IMMEDIATE 7988

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E.O. 11652: N/A

TAGS: ENRG, EINV, VE

SUBJECT: OIL NATIONALIZATION BILL

REF: CARACAS 2715 (B) CARACAS A-2847

1. THIS WILL BE THE FIRST OF SERIES OF CABLES ON THIS SUBJECT.
SPANISH TEXT OF BILL WHICH MINISTER OF MINES AND HYDROCARBONS
PRESENTED TO NATIONAL CONGRESS MARCH 11 BEING POUCHED AS ENCLOSURE
TO UNCLASSIFIED AIRGRAM TODAY, MARCH 13.

2. AS REPORTED IN REF A, GOV MODIFIED NATIONALIZATION BILL PREPARED
BY REVERSION COMMISSION IN A FUNDAMENTAL MANNER PRIOR TO SUB-
MITTING IT TO CONGRESS. ARTICLE FIVE OF THE COMMISSION BILL STATED
THAT OIL INDUSTRY ACTIVITIES COULD BE EXERCISED SOLELY BY THE NATIONA
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EXECUTIVE OR ENTITIES EXCLUSIVELY OWNED BY THE STATE. ARTICLE FIVE
OF THE BILL SUBMITTED TO CONGRESS CONTAINS A NEW CLAUSE WHICH STATES
THAT, IN SPECIAL CASES AND WHEN IT IS CONVENIENT TO THE PUBLIC
INTEREST, "ASSOCIATION AGREEMENTS" MAY BE MADE WITH PRIVATE
ENTITIES FOR A DETERMINED PERIOD AND WITH STATE PARTICIPATION

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SUFFICIENT TO GUARANTEE CONTROL, AND WITH PRIOR APPROVAL OF BOTH

CONGRESSIONAL BODIES. ARTICLE TWO OF THE BILL SENT TO CONGRESS ALSO ELIMINATES THE WORD "EXCLUSIVE" FROM THE COMMISSION DRAFTED SENTENCE THAT FOREIGN TRADE OF HYDROCARBONS SHALL BE UNDER THE EXCLUSIVE CONTROL OF THE STATE AND SUBSTITUTES THE WORDS "MANAGEMENT AND CONTROL OF THE STATE."

3. ARTICLE FIVE DREW INSTANT CRITICISM FROM THE POLITICAL OPPOSITION. PRESIDENT PEREZ, REFERRING SPECIFICALLY TO THE ARTICLE IN HIS ANNUAL REPORT TO CONGRESS, MARCH 12, STATED THAT HE WOULD NOT COMPROMISE ON THIS POINT. ARTICLE FIVE WILL PROVIDE THE LEGAL BASIS FOR OPERATING AGREEMENTS WITH THE PRIVATE OIL CONCESSIONAIRES AFTER NATIONALIZATION. NEW ARRANGMENTS FOR THE SERVICE CONTRACTORS, MOBIL AND OCCIDENTAL, CAN ALSO BE WORKED OUT UNDER THIS ARTICLE, SINCE THE GOV BILL DOES NOT EXEMPT SERVICE CONTRACTS FROM THE

NATIONALIZATION PROCESS.

4. THE INCLUSION IN ARTICLE ONE OF A 120 DAY GRACE PERIOD AFTER THE PASSAGE OF THE NATIONALIZATION LAW BEFORE THE PRIVATE CONCESSIONS TERMINATE SERVES TWO PURPOSES: IT PERMITS THE GOV TO ORGANIZE THE STATE HOLDING COMPANY THAT WILL ADMINISTER THE INDUSTRY, AND IT COULD PERMIT THE NATIONALIZATION LAW TO BE ENACTED EARLIER THAN ORIGINALLY ANTICIPATED. THERE ARE INDICATIONS THAT PRESIDENT PEREZ WILL MOVE QUICKLY TO HAVE THE NATIONALIZATION LAW ENACTED IN ORDER TO PREVENT POLITICAL DEBATE FROM BOGGING DOWN THE PROCESS, TO MAINTAIN THE ADMINISTRATION'S CONTROL OF THE SITUATION, AND AVOID WHATEVER EMBARRASSMENT THAT MIGHT RESULT SHOULD THE POLITICAL DEBATE CRIPPLE HIS NATIONALIZATION EFFORT. THE FOUR MONTH GRACE PERIOD WOULD PROVIDE TIME TO NEGOTIATE AGREEMENTS WITH THE PRIVATE COMPANIES. ALSO, IT IS POSSIBLE TO SPECULATE THAT THE GOV WILL NOT IN FACT RELIGIOUSLY FOLLOW THE IRON ORE COMPANIES NATIONALIZATION MODEL. IT WOULD BE PHYSICALLY IMPOSSIBLE, GIVEN THEIR OTHER RESPONSIBILITIES, FOR THE GOV NEGOTIATING TEAM TO CARRY OUT PROTRACTED NEGOTIATIONS WITH EACH OIL COMPANY TO THE SAME EXTENT THAT WAS DONE WITH US STEEL AND BETHLEHEM STEEL. WHAT THE GOV WILL MOST LIKELY DO IS APPLY SOME OF THE SAME PRINCIPLES IN NATIONALIZING THE OIL INDUSTRY THAT WERE ADOPTED WITH THE IRON ORE INDUSTRY; I.E., COMPENSATION TERMS, METHOD OF PAYING COMPENSATION (BONDS) AND OPERATING AGREEMENTS. BUT NATIONALIZATION MAY ACTUALLY COME FAIRLY SOON, WITH COMPANIES BEING TOLD THAT ACTUAL DETAILED LIMITED OFFICIAL USE

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NEGOTIATIONS WILL FOLLOW THE ACT.

5. THE QUESTION OF COMPENSATION, TOGETHER WITH THE GUARANTEE FUND OBLIGATION, MAY BE MORE CONTROVERSIAL THAN ORIGINALLY THOUGHT. FROM THE NET VALUE OF THE PROPERTIES, LESS THE ACCRUED AMOUNT OF DEPRECIATION AND AMORTIZATION, WHICH IS THE COMPENSATION BASE, CERTAIN DEDUCTIONS WILL BE MADE. THE SLEEPER DEDUCTION WILL BE THAT FOR THE VALUE OF PETROLEUM EXTRACTED BY THE EXPROPRIATED

CONCESSIONAIRES, OUTSIDE THE LIMITS OF THEIR CONCESSIONS, IN ACCORDANCE WITH VOLUMES ESTABLISHED IN AGREEMENTS OF UNITIZED EXPLOITATION OF RESERVOIRS ENTERED INTO WITH THE VENEZUELAN PETROLEUM CORPORATION (CVP). SINCE CVP CAME INTO EXISTENCE MANY YEARS AFTER SOME PRIVATE COMPANIES HAD BEGUN PRODUCING OIL FROM FIELDS THAT WERE SUBSEQUENTLY UNITIED UNDER AGREEMENTS WITH CVP, THE GOV COULD DEDUCT AN EXTREMELY LARGE VOLUME OF OIL THEORETICALLY OWNED TO CVP. IN OTHER WORDS, THE GOV CAN REDUCE COMPENSATION TO COMPANIES HAVING UNITIZATION AGREEMENTS WITH CVP BY WHATEVER AMOUNT IT CHOOSES. THE PRIVATE COMPANIES REFER TO THIS AS "DOUBLE DIPPING," MEANING THAT THE GOV GETS BOTH THE OIL REMAINING IN THE RESERVOIRS AFTER NATIONALIZATION AND WHATEVER QUANTITY THEY CHOOSE TO DEDUCT AS BEING "OWED" TO CVP FROM THAT ALREADY PRODUCED FROM THE RESERVOIRS

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OIL COMPANIES DO NOT NECESSARILY ANTICIPATE THAT THE GOV WILL CLAIM LARGE DEDUCTIONS, BUT THEY FEEL THE THREAT IS PRESENT. IN ANY EVENT, THE COMPANIES WILL NOT HAVE LONG TO WAIT AFTER NATIONALIZATION TO FIND OUT THE DECISION ON DEDUCTIONS, BECAUSE ARTICLE 12 REQUIRES THE GOV TO MAKE A FORMAL COMPENSATION OFFER WITH 45 DAYS AFTER THE LAW IS PASSED.

6. THE GUARANTEE FUND IS BASED ON AN ACCOUNTING FORMULA MUCH MORE ADVANTAGEOUS TO THE GOV THAN IS THE COMPENSATION FORMULA WITH RESPECT TO THE PRIVATE CONCESSIONAIRES. THIRTY DAYS AFTER THE LAW IS PROMULGATED THE OIL COMPANIES MUST MAKE A ONE TIME DEPOSIT TO THE FUND TO BRING IT UP TO A SUM EQUIVALENT TO TEN PERCENT OF CUMULATIVE GROSS INVESTMENT. SINCE MOST COMPANIES HAVE NOT PREVIOUSLY DEPOSITED SIGNIFICANT SUMS INTO THE FUND, ALTHOUGH MAKING PROVISION FOR PAYMENT IN THEIR RESERVE ACCOUNTS, THEY WILL BE REQUIRED TO PUT UP CONSIDERABLE CASH. IN THE CASE OF CREOLE PETROLEUM, A SENIOR COMPANY OFFICIAL ESTIMATED TO THE REPORTING OFFICER THAT HIS COMPANY WOULD HAVE TO PAY IN ABOUT \$135 MILLION TO THE FUND. SOME OIL COMPANY COMMENT HAS BEEN HEARD, NOT ENTIRELY IN JEST, THAT INSTEAD LIMITED OFFICIAL USE

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OF RECEIVING COMPENSATION FROM NATIONALIZATION, THEY COULD END UP IN A NET DEBTOR POSITION TO THE GOV. CERTAINLY, IF COMPENSATION IS PAID IN BONDS, THE OIL COMPANIES WOULD BE LAYING OUT MORE CASH INITIALLY THAN THEY WILL BE RECEIVING.

7. THE OTHER IMPORTANT PROVISION IN THE DRAFT BILL, WHICH REPRESENTS A CHANGE FROM THE COMMISSION VERSION, IS THE REDUCTION OF THE INTERIM SUPERVISORY COMMISSION MEMBERS FROM TWELVE TO NINE, SEVEN OF WHOM WILL BE DESIGNATED BY THE EXECUTIVE, AND TWO CHOSEN BY PRESIDENT PEREZ FROM A LIST OF THREE PROPOSED BY THE NATIONAL CONGRESS. THUS, THE PRESIDENT CAN ALMOST ENTIRELY CONTROL THE SUPERVISORY COMMISSION BY HIS SELECTION PROCESS.

8. FURTHER ANALYSIS FOLLOWS.
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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: PETROLEUM INDUSTRY, NATIONALIZATION, TEXT, LEGISLATIVE BILLS
Control Number: n/a
Copy: SINGLE
Draft Date: 13 MAR 1975
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: GolinoFR
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1975CARACA02847
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Film Number: D750088-0874
From: CARACAS
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1975/newtext/t19750355/aaaabxlz.tel
Line Count: 169
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION ARA
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 4
Previous Channel Indicators: n/a
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: 75 CARACAS 2715, 75 CARACAS A-2847
Review Action: RELEASED, APPROVED
Review Authority: GolinoFR
Review Comment: n/a
Review Content Flags:
Review Date: 12 SEP 2003
Review Event:
Review Exemptions: n/a
Review History: RELEASED <12 SEP 2003 by izenbei0>; APPROVED <29 OCT 2003 by GolinoFR>
Review Markings:

Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
05 JUL 2006

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: OIL NATIONALIZATION BILL
TAGS: ENRG, EINV, VE
To: STATE
Type: TE
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 05 JUL 2006